

complaint

Mr J has complained that advice he received from HSBC Bank Plc (“HSBC”) in July 2004 to invest £50,000 across two Open Ended Investment Companies (OEIC) based on a ‘medium’ attitude to investment risk was unsuitable for him.

He is represented by a third part adviser, which has said that:

- the adviser failed to fully establish his circumstances at the time of the sale.
- he was pressured into meeting an adviser after he inherited £31,000.
- he had an outstanding mortgage but was not advised to repay this first.
- he was advised to borrow a further £19,000 to increase his investment to £50,000.
- he was not left with a sufficient cash reserve.
- the adviser failed to establish his attitude to risk as he clearly stated that he could not afford to lose money and did not want to take any risk with his inheritance.
- he was not told that this capital was at risk.

Mr J surrendered the investment in February and March 2009 for a significant financial loss and has requested HSBC to compensate him for these losses.

background

Mr J’s complaint was considered by one of our adjudicators who concluded that it should be upheld because he considered that the investment funds recommended included a substantial equity content which represented a higher level of risk than Mr J had previously taken with his savings.

The adjudicator also considered that the attitude to risk rating of ‘medium’ did not seem to be consistent with his previous investment experience which was predominantly held in deposit based accounts.

While Mr J held substantial assets following a recent inheritance, it did not necessarily follow that he was willing to take a significant risk with money he had only just inherited less than ten years before he anticipated retirement.

Following the advice Mr J received, the proportion of his total capital invested in risk-based product increased from just over one per cent to around 52 per cent. In the adjudicator’s opinion, although Mr J wanted capital growth, there was little justification for placing his available capital in a significantly more risky environment than the products in which it had previously been held.

Also, the adjudicator did not feel that the risks posed by this investment were adequately explained to Mr J or that he understood them.

In response, HSBC disagreed with the adjudicator’s assessment and said that:

- Mr J actually invested £10,000 in the British Fund, and not £20,000 as the adjudicator stated;
- the recent increase in his capital savings due to an inheritance of just over £30,000 would have changed Mr J’s previous approach to investment;

- he was in his mid-50s, widowed and had no financial dependants, with almost ten years to retirement. He did have some investment experience as he was already contributing to a stocks and shares ISA on a monthly basis;
- the funds were recommended to provide diversification, which Mr J felt was sufficient for his personal needs and that there was greater growth potential by investing in equities and bonds;
- an "Investment Planner Calculation Sheet" completed by the adviser following his recommendation shows that Mr J's revised portfolio was within HSBC's guidelines for a 'balanced' investor. The total Mr J held in 'balanced' holdings was also only 2% greater than the amount that was considered appropriate for a 'cautious' investor;
- Mr J completed and signed the customer declaration on the 'factfind' confirming that he had the opportunity to read the information gathered, that it was complete and accurate and that the risks had been explained to him;
- in April 2005 HSBC changed the risk rating of one of the funds - the European Growth Fund - from 'balanced' to 'adventurous'. This would have been communicated to Mr J in the Investment Report issued at the time, which advised investors to contact their financial adviser if the fund no longer met their requirements. As there is no evidence of Mr J taking any action regarding this, it would appear that he was satisfied with the fund at that time.

In response, the adjudicator said that:

- while he agreed that Mr J now had additional funds to invest following an inheritance, it did not follow that he was prepared to take a 'medium' approach to investment risk with that inheritance;
- Mr J's existing stocks and shares ISA amounted to only just over one per cent of his total available funds, with the majority of his savings being in secure holdings. This appears to be indicative of an investor with a 'risk-averse' or 'low-to-cautious' attitude to investment;
- whether or not Mr J's spread of investments following the advice was within HSBC's guidelines for a 'balanced' investor, it is doubtful whether a 'risk-rating' of balanced truly reflected Mr J's circumstances at the time and limited investment experience.
- there is little evidence to explain why Mr J switched from being a 'risk-averse or 'low/cautious' investor to one with a balanced attitude to investment risk;
- that Mr J acquired additional funds through an inheritance does not mean that he would have been prepared to take an investment risk with those funds.

As no agreement could be reached in this complaint, it has been referred to me for review.

my findings

I have considered all the available evidence and arguments to decide what is fair and reasonable in the circumstances of this complaint.

My understanding of Mr J's personal and financial circumstances in July 2004 is that he was in his mid-50s, widowed and earned over £30,000 per annum with no financial dependents. Although he anticipated retirement at age 65, in approximately nine years' time, he had no personal pension provision in place. His earnings gave him a net disposable income of more than £400 per month.

Before he inherited around £30,000, his total capital savings amounted to almost £68,500 of which all but approximately 2% - invested in a stocks and shares ISA worth £1,300 - was held in capital secure deposit accounts.

Following the advice he received, it appears that Mr J's savings portfolio comprised approximately 48% in capital secure accounts, 20% in 'cautious' risk-rated funds and 32% in 'balanced' holdings. Although Mr J's representative has said that he was advised to take a further loan to increase his investment to £50,000, I have not seen any evidence to support this aspect of Mr J's complaint as the whole of the capital sum invested appears to have come from his existing savings.

However, I am not persuaded how an inheritance of approximately £30,000, when added to already significant capital savings that were all but held in capital secure accounts, should change Mr J's investment approach so radically from 'risk-averse' to 'medium'.

It is likely that, when Mr J came to retire in approximately nine years' time, his income would reduce and he would then be dependent on his savings to replace this lost income. In these circumstances, I believe an overriding consideration for him was to ensure that his capital remained predominantly secure until such time as he needed to call on it to replace his income from employment.

While his attitude to risk at the point of sale was established as 'medium', there is no meaningful discussion or method documented in the fact find to explain *why* Mr J should adopt a 'medium' risk approach to investment. The definition of a 'medium' attitude to risk set out by the adviser did explain that Mr J must take a risk if he wants to achieve greater returns than might be available from deposit-based accounts but this does not justify why Mr J should, or could afford to, take this degree of risk in his circumstances.

My view is that, based on the nature of the investments previously held by Mr J, I would not regard him as a 'medium' risk investor simply because he had acquired a further £30,000 through an inheritance.

On balance, I do not consider it likely that, with nine years to retirement, Mr J would be prepared to expose over 50% of his total capital to the degree of risk represented by these two investments. As Mr J was also widowed, and his earning capacity was likely to reduce when he retired, he was in a position where he could ill-afford to take any risk with his savings as he had little evident means of recouping any potential investment losses in the future.

Furthermore, I am conscious that Mr J was approximately nine years from his anticipated retirement date and he had no pension provision in place at all. I do not believe that it was appropriate, therefore, for him to expose a significant proportion of more than 50% of his total capital savings to either a 'cautious' or 'balanced' degree of risk with only nine years to go to retirement.

On balance, if Mr J's objective was to achieve a return on this part of his capital savings that could exceed the interest he would receive from deposit-based account, I am inclined to believe that he should have received advice on the basis that he wished to adopt, at most, a wholly 'cautious' attitude to risk.

I do note that Mr J took significant capital withdrawals of approximately £23,500 from the two in less than four years he held which could suggest that he was not reliant on these savings

for retirement. However, it is equally plausible that Mr J did not appreciate that these capital withdrawals would have such an adverse effect on the on-going value of these investments.

fair compensation

In assessing what would be fair compensation, I consider that my aim should be to put Mr J as close to the position he would probably now be in if he had not been given unsuitable advice.

I take the view that Mr J would have invested differently. It is not possible to say *precisely* what he would have done differently. But I am satisfied that what I have set out below is fair and reasonable given Mr J's circumstances and objectives when he invested.

what should HSBC do?

To compensate Mr J fairly, HSBC must compare the performance of Mr J's investments with that of the benchmark shown below.

The compensation payable to Mr J is the difference between the *fair value* and the *actual value* of Mr J's investment. If the *actual value* is greater than the *fair value*, no compensation is payable.

A separate calculation should be carried out for each investment.

HSBC should also pay Mr J any interest, as set out below. Income tax may be payable on the interest awarded.

investment name	status	benchmark	from ("start date")	to ("end date")	additional interest
OEIC H023071	surrendered	for half the investment: FTSE WMA Stock Market Income Total Return Index; for the other half: average rate from fixed rate bonds	date of investment	date surrendered	8% simple p.a. on any loss from the end date to the date of settlement
OEIC H024315	surrendered	for half the investment: FTSE WMA Stock Market Income Total Return Index; for the other half: average rate from fixed rate bonds	date of investment	date surrendered	8% simple p.a. on any loss from the end date to the date of settlement

For each investment:

actual value

This means the actual amount paid or payable from the investment at the end date.

fair value

This is what the investment would have been worth at the end date had it produced a return using the benchmark.

To arrive at the *fair value* when using the fixed rate bonds as the benchmark, HSBC should use the monthly average rate for the fixed rate bonds with 12 to 17 months maturity as published by the Bank of England. The rate for each month is that shown as at the end of the previous month. Those rates should be applied to the investment on an annually compounded basis.

Any withdrawal, income or other payment out of the investment should be deducted from the *fair value* at the point it was actually paid so it ceases to accrue any return in the calculation from that point on.

If there are a large number of regular payments, to keep calculations simpler, I will accept if HSBC totals all those payments and deducts that figure at the end instead of deducting periodically.

why is this remedy suitable?

I have decided on this method of compensation because Mr J wanted capital growth with a small risk to his capital.

The average rate for the fixed rate bonds would be a fair measure for someone who wanted to achieve a reasonable return without risk to his capital.

The WMA index is a mix of diversified indices representing different asset classes, mainly UK equities and government bonds. It would be a fair measure for someone who was prepared to take some risk to get a higher return.

I consider that Mr J's risk profile was in between, in the sense that he was prepared to take a small level of risk to attain his investment objectives. So, the 50/50 combination would reasonably put Mr J into that position. It does not mean that Mr J would have invested 50% of his money in a fixed rate bond and 50% in some kind of index tracker fund. Rather, I consider this a reasonable compromise that broadly reflects the sort of return Mr J could have obtained from investments suited to his objective and risk attitude.

The additional interest is for being deprived of the use of any compensation money since the end date.

my final decision

My final decision is that I uphold Mr J's complaint.

I require HSBC Bank Plc should pay Mr J the amount calculated as set out above.

Also, HSBC Bank Plc should provide details of its calculation to Mr J in a clear, simple format.

Kim Davenport
ombudsman